

# **City of Chelsea**

## **Five Year Financial Forecast for Fiscal Years 2009-2013 and Preliminary FY'09 Budget Overview**

to be Presented to the City Council

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# Five Year Financial Forecast

## Revenue and Expenditure Summary

	FY'09	FY'10	FY'11	FY'12	FY'13
Revenue \$	117,573,903	119,579,621	123,038,843	126,126,556	126,929,367
% Change	2.86%	1.71%	2.89%	2.51%	0.64%
Expenditures \$	118,221,672	120,455,331	123,604,778	126,442,584	126,686,821
% Change	3.43%	1.89%	2.61%	2.30%	0.19%
Surplus / (Deficit)	(647,769)	(875,710)	(565,935)	(316,028)	242,546

# Understanding the Numbers

## REVENUES

- House 1, Governor Patrick's State Budget recommendation for FY'09, and subsequent announcements from both the House and Senate indicate that level funding will occur for both Lottery Aid and Additional Assistance, as well as an increase in Chapter 70 School Aid. The local impact is:
  - Lottery Aid will remain at \$6,824,838
  - Additional Assistance will remain at \$3,396,864
  - Chapter 70 School Aid will increase 4.70%, or by \$2,280,218, to \$50,797,335
- The future of Local Aid for FY'10-'13 is difficult to predict. For planning purposes the City is assuming for those years: no increase in Additional Assistance, a 3% annual average increase in Lottery Aid beginning in FY'11 and a 2.5% annual average increase in Chapter 70 School Aid.
- Tax Levy and Levy Limit are projected to grow by 2.5% plus New Growth. New Growth projections are increasing substantially as a result of pending residential development activity. The Overlay provision is reduced to 1.5% of the prior year levy, reflecting historical usage.
- Fines & Forfeits projections are reduced based upon the experiences of previous years, while Licenses & Permits are expected to fluctuate at higher levels as a result of building fees associated with the pending residential development activity. Trash fees are expected to rise in the area of 5% yearly.
- Interest on Investment is projected to remain at current levels.

# Understanding the Numbers

## EXPENSES

- Salary Costs reflect a 1% increase on the last day of FY'08, which has a financial impact on the first day of '09, plus an assumption of increases of 2.5%, 2.5% and 3% for FY'09-'11, and a 2% increase in each of FY'12 and FY'13. The assumed increases are for planning purposes and subject to negotiation with the City's various bargaining units. All current contracts expire at the end of FY'08, so negotiations will begin shortly with several bargaining units for new, three year contracts.
- Health Insurance rates will increase by approximately 7.0%, including schools, for FY'09. Costs are projected to increase by 10.0% annually thereafter.
- Retirement costs are up for both City and Schools per the PERAC schedule at an average 4.3% over the 5 years. It is anticipated that the City cost only of Retirement will increase by 4.8%.
- Overall spending is projected to increase by 3.4% in FY'09. In FY'09, Education spending is projected to increase by 3.9%, while Non-School spending is projected to increase by 2.9%. The Operating Budget, considered Non-School expenses minus Employee Benefits, Debt Service and Assessments, is projected to increase in 2.6% in FY'09.
- The State Assessment for Charter Schools is increasing dramatically (up \$353,610), although the increase is moderated, in part, by increased State Aid for Charter Schools (up \$102,463).
- Debt Service is based upon current and future infrastructure related costs. The retirement of new schools loans will take place in 2016. Debt service, minus school loans, is generally unchanged in the short-term and trending downward.

# Budget Pressures

## SUMMARY

- After a period of moderate economic growth, speculation abounds that the economy is now in recession. Unfortunately, the State and many of its municipalities are still trying to recover from the last recession. Difficult public budgeting times appear to be prolonged, extending out what may be the worst municipal finance period in a half century or longer.
- What appears to be a chronic State budget crisis continues to have negative direct and indirect impacts on municipalities budgets, including the City's. The most significant of those direct impacts is the status of Local Aid, as an anticipated level funding of Lottery Aid and continued suppression of Additional Assistance will keep non-school Local Aid below FY'01 highs.
- Although the City does not receive much in the way of Federal funding, the previous loss of Weed & Seed funding and now potential changes to Medicare reimbursements continue to have a negative impact on Federal revenue accounts.
- Despite the City's ability to control discretionary spending, Employee Wages and Benefits, most notably Health Insurance and Retirement, continue to rise at rates well beyond inflation.
- Health Insurance will continue to increase significantly. Agreement on joining the State's health insurance system has not been reached with local unions, although the State is talking about mandating that communities join the system or vesting the decision with management.
- Retirement assessments, aimed to recover from the lack of funding provided over decades of mayoral administrations, are substantially greater than the projected budget gaps.

# Budget Pressures

## SUMMARY (continued)

- The City has likely exhausted significant cost-cutting measures, and may only be able to rely upon significant service rollbacks, including, for example, taking a fire piece out of service, reducing library hours or closing the senior center, if other expenditures cannot be controlled and revenues do not increase.
- While employee wages are held in check through FY'08, it is not reasonable to expect that employee unions will continue to accept nominal wage increases too far into the future. As a result, the City is projecting higher employee wage costs over the next three years.
- Non-school Local Aid remains below FY'01 highs, and below FY'84 levels when adjusted for inflation, while other non-property tax revenues, including excise tax and Payments In Lieu Of Taxes (PILOT) receipts, remain stagnant, thereby not growing sufficiently enough to eliminate projected deficits.
- Free Cash and other reserves continue to dwindle, as previous budget deficits, even after budget cutting and revenue enhancing, have needed to be eliminated.
- As reserves dwindle, the City's financial flexibility becomes more restricted.
- Without success on an aggressive economic development plan and adoption of the State health insurance option, one or a combination of three occurrences may need to take place to balance out-year budgets: a depletion of Stabilization balances, deep service cuts and/or a Proposition 2 ½ Override.
- Fortunately, fiscal discipline is holding deficits down while success on the aggressive economic development agenda appears able to generate building fees and property tax growth sufficient enough to eventually provide a structurally balanced budget in FY'13. Health insurance discussion are ongoing.

# Budget Pressures

## BUDGET BUSTERS FY'08 - EXPENDITURES

In addition to the budget expansion caused by wage increases, contracts for service, supplies, energy and the like, “Budget Busters” have historically had a significant impact on the City’s budgets. In FY’09, the impact of Budget Busters will be:

- Health Insurance, which will *rise* 7.00%, or \$400,327, for the City (not including Schools). Employees are now paying 15% towards HMO coverage, with the small number choosing an indemnity plan paying 25%. The City, like most other entities, public or private, continues to grapple with real or projected double-digit increases and searches, with varying success, for substantive relief. Absent the City finding savings by joining the State health insurance system, pressure will continue to mount for an increase in employee premiums to 17.5%; an increase in retiree health insurance premiums, maybe to 25%; a reduction of services; a further reduction in reserves, and/or other fiscal stress.
- Retirement costs to the City are scheduled to *rise* by 5.1% or \$253,780, in FY’09. In the out years, the anticipated annual 4.8% increase will outpace the overall budget growth.
- School Choice & Charter School Assessments are *up* a net \$348,610, or 18.4%, as a result of increased out-of-district enrollments. The net amount includes offsets as a result of additional State reimbursements.
- The Northeast Regional Vocational School Assessment is forecast to increase by 19.9%, or \$136,391, although the City and other member municipalities are engaged in discussion with school leadership on reducing the school’s budget, and, therefore, the Voke school’s assessment to member communities.

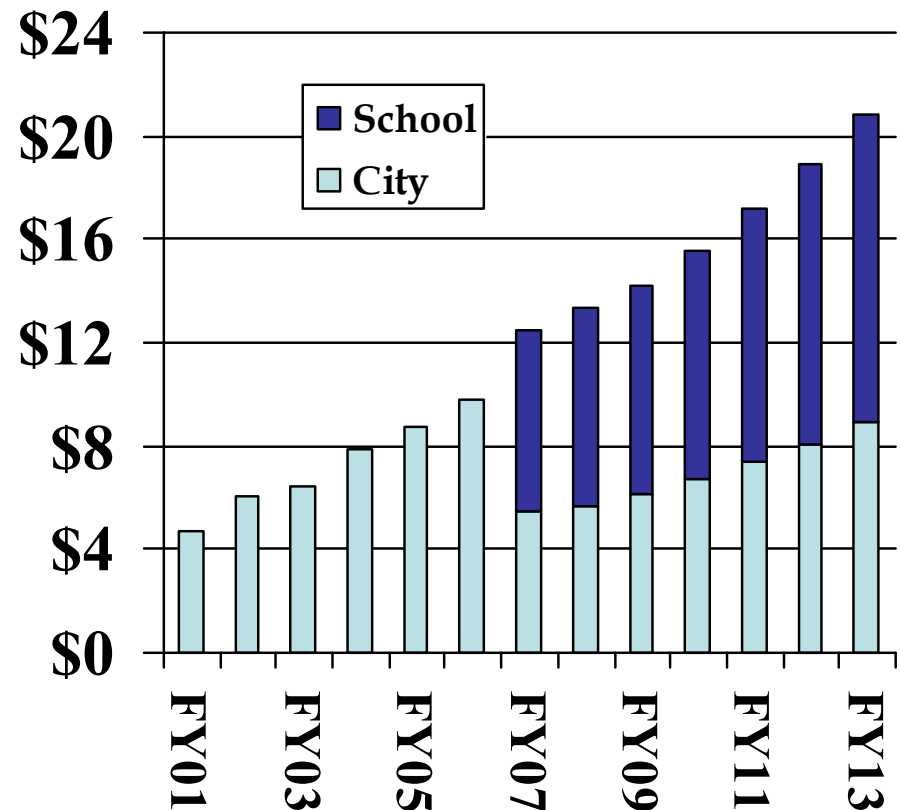
# Budget Pressures

## Expenditures:

- By contract, the City covers 85% for HMO (down from 90% prior to FY'08) and 75% of Indemnity and Medex costs for employees. The same coverages are provided for eligible retirees.
- In addition, the City has previously attempted to control costs by joining the City of Boston's health insurance system, agreeing to higher co-pays and deductibles, as well as reducing the overall number of plans offered.
- Despite those efforts, Health Insurance has risen \$9.5 million, for an average combined 11.9% increase, from FY'01-FY'09 for the City and Schools.
- For FY'09, Health Insurance costs will increase by a projected 7.0% for the City.
- In the out years, the City is forecasting increases of 10.0% annually.
- Negotiations continue with local municipal union leaders to consider abandoning the current health insurance procurement in favor of joining the State's Group Insurance Commission. The City estimates such a move could cut overall health insurance costs by 15%.

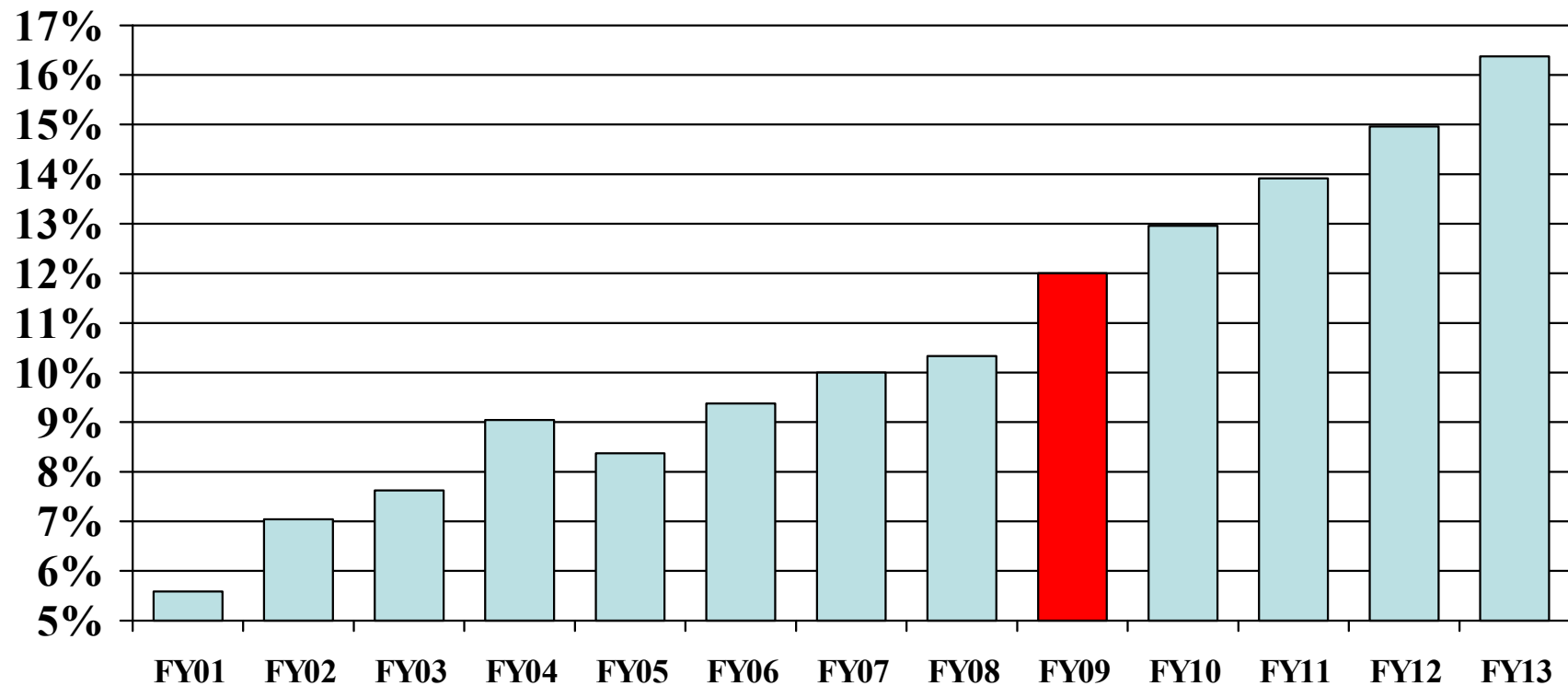
## Health Insurance Costs

amounts in millions - net of employee contributions



# Budget Pressures

## Health Insurance as Percent of Total Budget

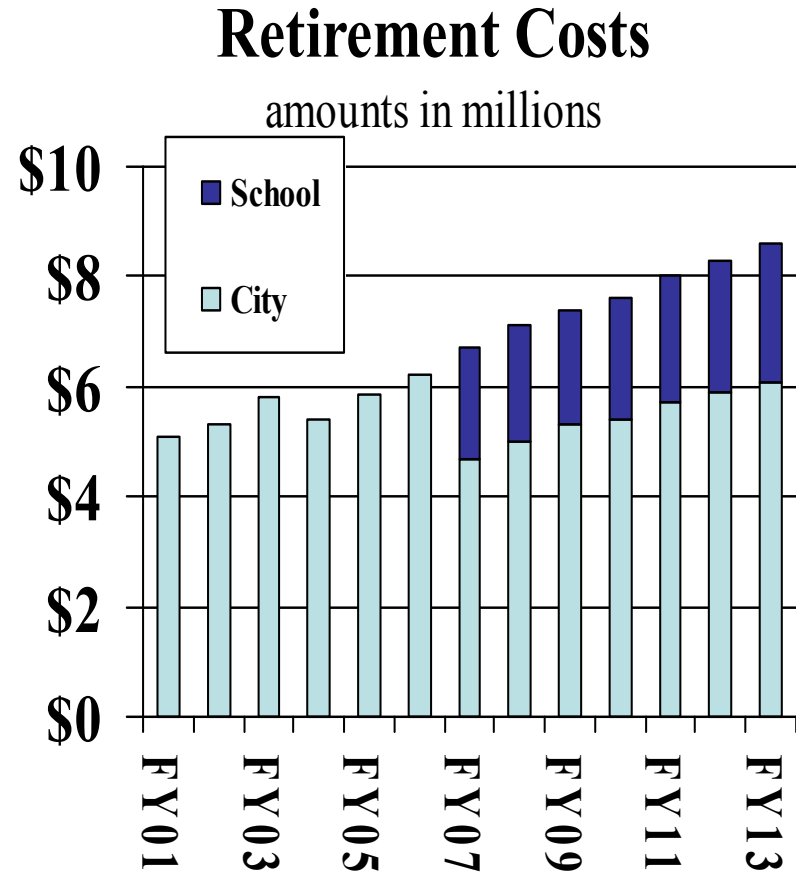


*Reflects combined City and School expenditures*

# Budget Pressures

## Expenditures:

- The City is required to make annual payments into its Retirement System as a benefit to employees.
- Payments are based upon a schedule which seeks to have the City's under-funded system fully funded by 2025, three years earlier than State law requires and reflective of the fund's earning performance.
- 81.2% of the total FY'09 charge, or \$5,953,180, is a "catch-up" payment required as a result of the failure of past mayoral administrations to provide for retirement costs.
- Catch-up payments continue to grow into 2025, including \$6,831,411 for FY'13 and \$10,322,730 in FY'25.
- Retirement costs, including schools, has increased by an average of 5.6% from FY'01 to FY'09.
- For FY'09, Retirement is projected to increase by 3.8%, or \$267,104, including schools, and 5.1%, or \$253,780, for the City only.
- For the period FY'09-'13, Retirement, including schools, will increase on average by 4.3%, and 4.8% for the City only.



# Budget Pressures

## BUDGET BUSTERS (NON-SCHOOL) FY'09 - EXPENDITURES

- Health Insurance up 7.0% \$400,327
- Retirement (City only) up 5.1% \$253,780
- School Choice/Charter up 18.4% \$348,610
- Northeast Voke, up 19.9% \$136,391

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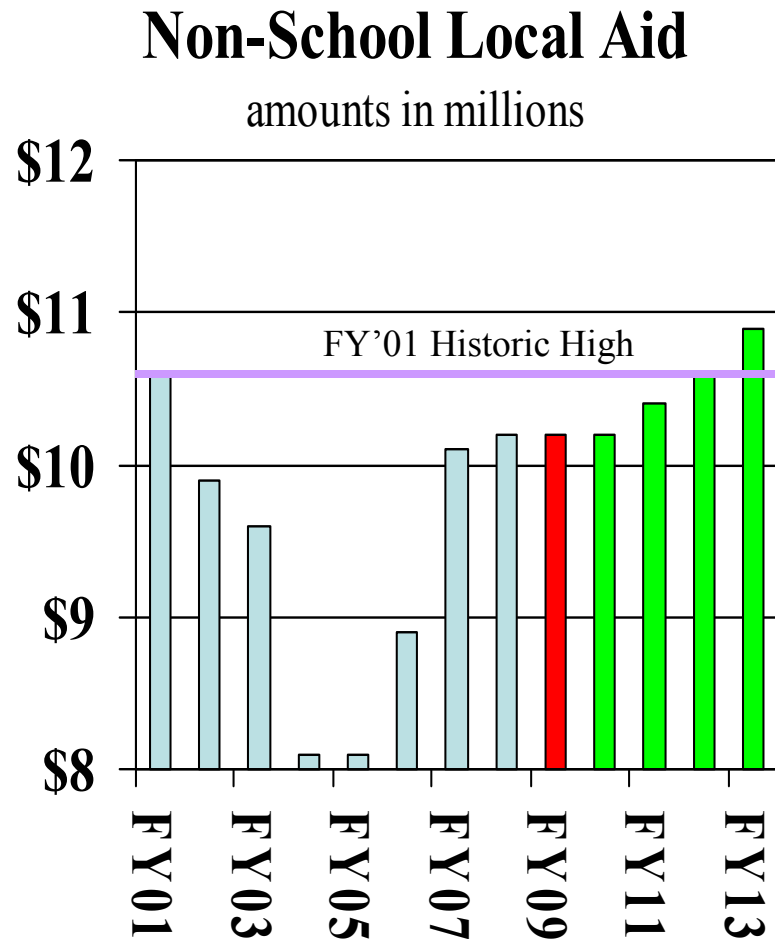
**TOTAL    \$1,139,108**

By comparison, FY'09 Property Taxes are up \$1,732,841

# Budget Pressures

## Revenues:

- Non-school Local Aid provides funding for general municipal services.
- The two greatest sources of non-school Local Aid are Lottery Aid and Additional Assistance.
- For FY'09, the State is proposing no increase to non-school Local Aid.
- For FY09, the total aid of \$10.1m is \$405,655 less than FY'01, or 96% of the historic high for the two accounts.
- The cumulative loss in non-school Local Aid revenue from the FY'01 high through FY'09 is \$9.7m (meaning that \$9.7m in Free Cash has been used to make up for Local Aid shortages).
- Adjusted for 2.5% inflation, non-school Local Aid is down \$2.7m for FY'09, far eclipsing the City's proposed deficit.
- The City projects that the FY'01 historic high may not be reached again until FY'12, unadjusted for inflation.



# Budget Pressures

## BUDGET TRENDS FY'09 & BEYOND

On the positive:

- The City's fiscal discipline continues to provide for budget stability.
- The City's management of reserves continues to allow for the maintenance and expansion of critical services while budgets remained balanced.
- Major economic development initiatives, including the City's 1,200-unit housing goal, are promising, thereby providing the potential for increasing new growth and building permit fees to offset otherwise looming deficits.
- Debt Service is declining.

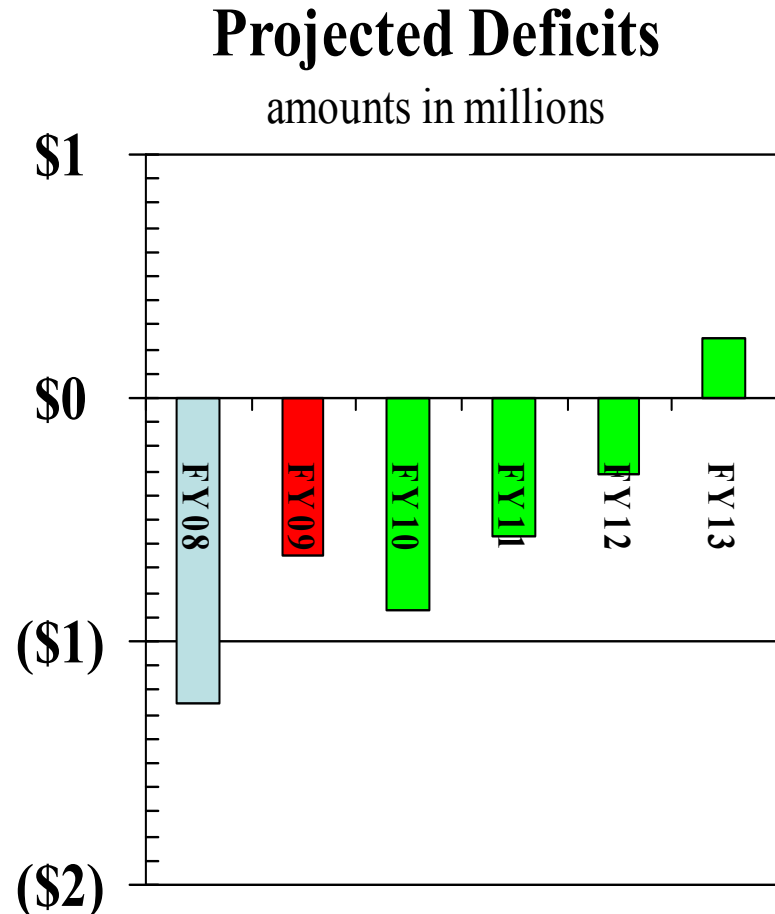
On the negative:

- Another recession may be occurring, and the City is less financially prepared to deal with serious financial consequences should such occur because the "growth" years failed to produce dramatic revenue growth to allow the City to replenish reserve levels.
- Local Aid is stagnate and still below historical absolute and time adjusted highs.
- Locally raised revenues must grow at rates necessary to offset static Local Aid levels and increasing spending requirements, especially non-discretionary spending.
- Health Insurance is increasing 7% (City and Schools combined) for FY'09, and has increased an average of 11.9% for the years FY'01-'09.
- Both Health Insurance and Retirement costs will continue to grow beyond general budget growth, meaning employee benefits will continue consuming larger portions of the City's annual spending.
- Merited labor wage increases may be unsustainable as they impact projected structural deficits.
- Free Cash continues to dwindle, reducing budget flexibility and potentially impacting core municipal services.

# Budget Pressures

## FIVE YEAR DEFICITS:

- Should no action be taken, deficits do exist in each of the next four years, with a surplus being reduced in year five:
  - FY'09 (\$ .648 M)
  - FY'10 (\$ .876 M)
  - FY'11 (\$ .566 M)
  - FY'12 (\$ .316 M)
  - FY'13 \$ .243 M
- The deficits are primarily a result of sluggish Local Aid growth, and skyrocketing Employee Benefit costs.
- The deficits reflect City success in attracting 1,200+ residential units, partially taxable beginning in FY'09.
- The City is not alone in projecting deficits. Many other municipalities are experiencing similar budgetary pressures, or worse.
- Local management has resulted in fund balances available to offset deficits.



# Budget Pressures

## Deficits compared to increases in Health Insurance and Retirement costs

<u>FY'09</u>	<u>FY'10</u>	<u>FY'11</u>	<u>FY'12</u>	<u>FY'13</u>
Projected Deficits				
(\$647,769)	(\$875,710)	(\$565,934)	(\$316,027)	\$242,545
Health Insurance Increases (Projected FY'09-'13)				
\$400,327	\$611,928	\$673,120	\$740,433	\$814,476
Retirement "Catch-Up" Charges (Projected FY'09-'13)				
\$5,953,180	\$6,161,541	\$6,377,195	\$6,600,397	\$6,831,411

# Deficit Reduction Plan

## 1,200-Unit Goal

- The City established a goal of promoting the development of at least 1,200 units to, in part, expand the local tax base. Since that goal was announced in 2005, targeted economic development activity has led the City to meet and exceed the target set. The following discusses the various housing projects contemplated or underway in the city, the status of those projects, the anticipate one-time building fees associated with the projects and the anticipated property tax growth the projects are expected to contribute:

Project	Units	Status	Building Fees	Property Taxes
Forbes Phase I	64	Under Construction	<i>\$100,000</i>	\$160,000
Atlas Phase I	60	Near Complete	<i>\$95,000</i>	\$135,000
Parkway Plaza	238	Near Complete	<i>\$500,000</i>	\$600,000
Forbes Phase II	70	Permitted	\$175,000	\$210,000
Atlas Phase II	60	Under Construction	\$126,000	\$135,000
Admirals Hill	160	Under Construction	<i>\$345,000</i>	\$400,000
Urban Ren. Phase I	280	Permitted	\$500,000	\$700,000
Scattered Sites	200	Various	\$500,000	\$450,000
Webster Block	141	Pre-Permitting	\$250,000	\$282,000
Forbes III	164	Planning	\$420,000	\$492,000
Urban Ren. Phase II	250	Pre-Planning	\$600,000	\$750,000
TOTAL	1,687		\$3,608,000	\$4,314,000

*Italics indicate funds already received*

# Deficit Reduction Plan

## Impact of 1,200-unit goal on Projected Deficits

FY'09	FY'10	FY'11	FY'12	FY'13
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Deficit with 1,200-unit goal (Numbers reflect 1687 units taxable by FY'13)

(\$647,769)	(\$875,710)	(\$565,934)	(\$316,027)	\$242,545
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Deficit without 1,200-unit goal (Numbers reflect no new units)

(\$1,752,769)	(\$1,881,710)	(\$2,874,934)	(\$2,852,027)	(\$3,305,955)
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# Projected Use of Reserves

	<u>FY'08</u>	<u>FY'09</u>	<u>FY'10</u>	<u>FY'11</u>	<u>FY'12</u>	<u>FY'13</u>
<b>General Fund</b>						
Free Cash Certified at Start of Year	4,610,537	4,212,768	3,587,058	3,271,124	3,205,097	3,455,097
Free Cash Used for Budget Gap	(647,769)	(875,710)	(565,934)	(316,027)	0	0
Supplemental Appropriations from Free Cash	(250,000)	(250,000)	(250,000)	(250,000)	(250,000)	(250,000)
Accounting and Managerial Activities	0	0	0	0	0	242,545
Year's Net Activities Affecting Free Cash	500,000	500,000	500,000	500,000	500,000	500,000
Free Cash Estimated at Year End	4,212,768	3,587,058	3,271,124	3,205,097	3,455,097	3,947,642
<b>Stabilization Balance at start of year</b>						
General 7020	3,656,270	3,802,521	3,954,622	4,112,806	4,277,319	4,448,412
Capital 7022	849,520	883,501	918,841	955,594	993,818	1,033,571
Planning & Development 7021	142,355	148,049	153,971	160,130	166,535	173,197
<i>assuming a 4% investment return</i>						

# Potential Future Budget Impacts

## ON THE POSITIVE

- The City was not one of the 20% of communities that needed to seek a Proposition 2 ½ Override in 2007.
- Switching to the State's health insurance system could save 10-15% of the health insurance base, and lead to smaller annual increases.
- The City is active in statewide policy discussions that could lead to reduced impacts from retirement and charter school costs, as well as lead to a regionalization of services to maintain and improve efficiencies while saving costs.
- Ongoing discussions regarding future PILOTs could lead to an increase in those revenues.
- Promising economic development could lead to further increases in building fees, property taxes, hotel/motel excise taxes and motor vehicle excise taxes.

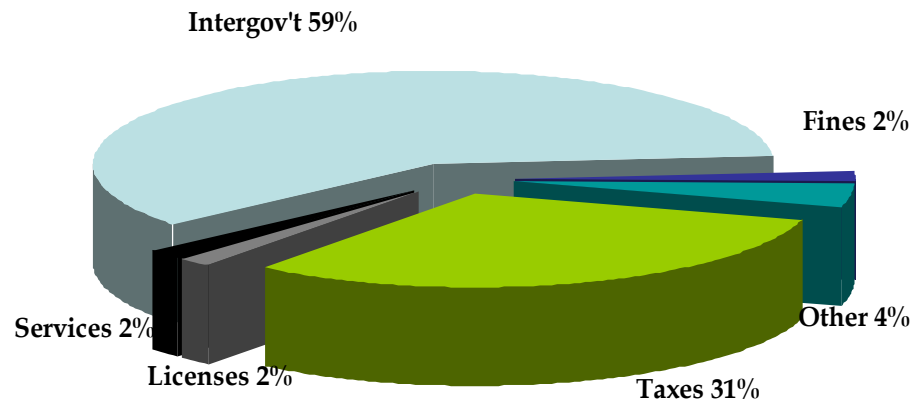
## ON THE NEGATIVE

- Failure to produce on the aggressive economic development agenda could leave substantial budgetary gaps.
- The lingering State budget crisis and current recession could lead to further local aid reductions and other revenue impacts.
- Motor Vehicle Excise Tax receipts could be reduced if local airport related parking is negatively impacted by future airport and airline issues.
- A new round of collective bargaining for FY'09-FY'11 cannot result in pay increases beyond the budget's ability to afford those increases.
- Federal reductions in Medicare reimbursements could result in funding shortfalls to support necessary school health programs.
- Utility costs continue to skyrocket.
- Failure to replenish reserves could require dramatic service impacts or a need for a Proposition 2 ½ Override if the current economic downturn is prolonged.
- Uncertainty in municipal bond markets may make borrowing costs to support necessary infrastructure projects more expensive.

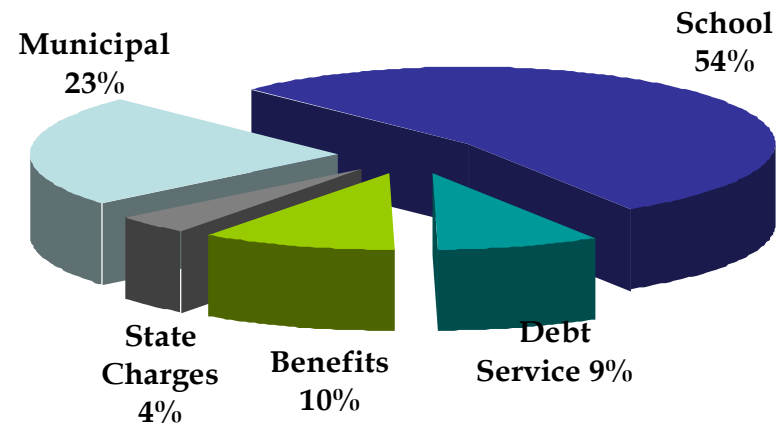
# FY'09 Budget

## General Fund Revenue & Expenses

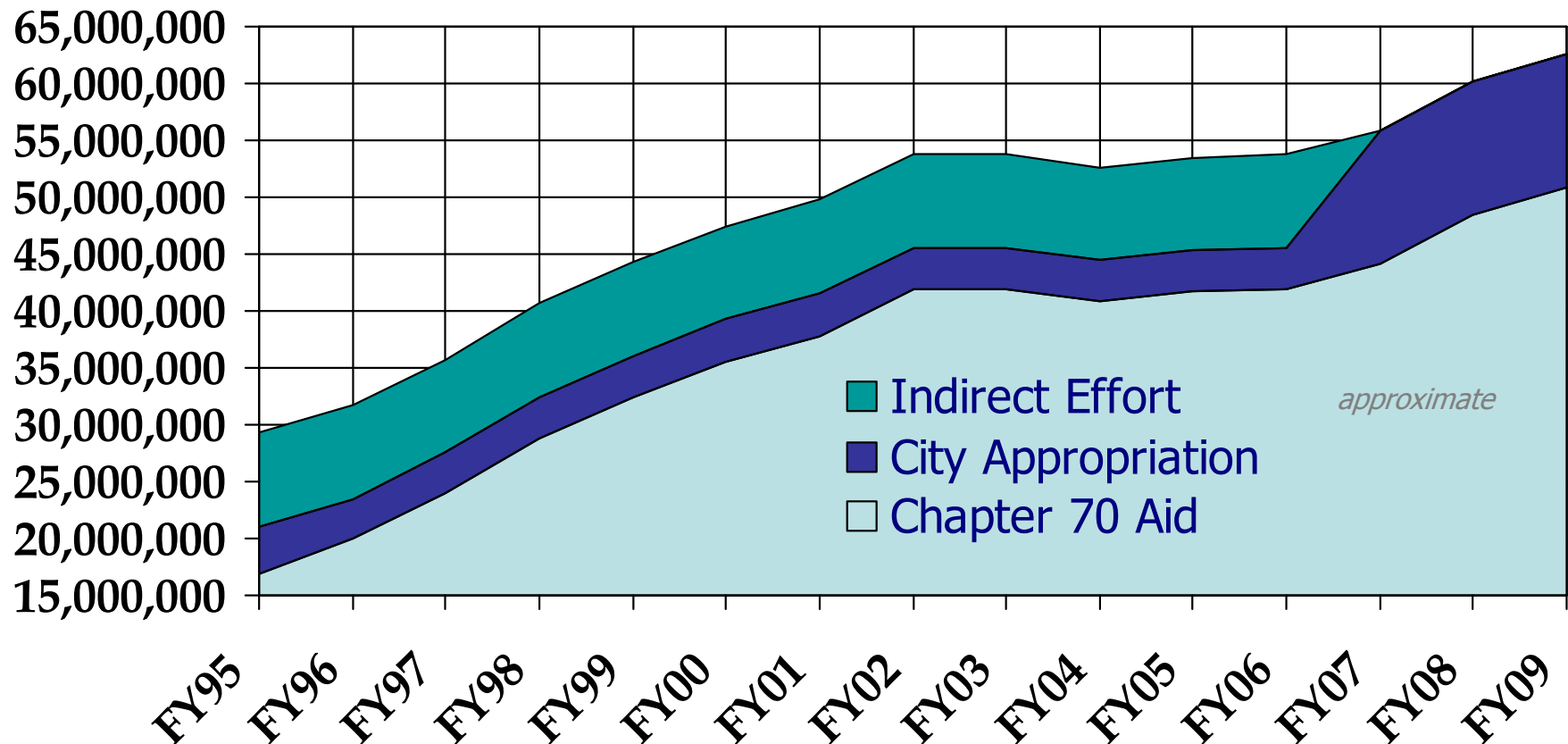
Revenue



Expense



# School Department Funding



# Water and Sewer Enterprise Funds

- As Enterprise Funds, all costs associated with water and sewer services shall be recouped through Water and Sewer revenues.
- The largest revenue source for the Funds are user fees, which account for 99% of the \$13,492,101 that will be raised in FY'09.
- The largest expense for the Funds are the annual MWRA Assessments, a formula driven charge. Preliminary Assessments indicate a 5.8% combined increase in MWRA assessments for FY'09. The MWRA Assessments comprise 57.8% of expenses for the funds, for a total of \$7,792,645.
- Other charges to the funds include direct expenses to pay the RH White maintenance contract and other charges, indirect expenses to pay for other employee allocation costs of the General Fund, and debt services to pay for the continuing update of water and sewer infrastructure.
- The City projects that future rate increases, inclusive of MWRA Assessments and Debt Service to pay for continuing water, sewer and drainage infrastructure improvements, will be 9.0% for FY'09, and 6.5% thereafter. The 9.0% increase has already been levied.
- The larger, 9.0% increase, was required to cover shortfalls that were the result of the City's assessment model leading to under-billing for full cost recovery. The under-billing left a manageable deficit which the new rates are meant to alleviate.

# Municipal Costs Affordability Index

- The City reviews data from 7 neighboring cities (Boston, Everett, Lynn, Malden, Revere, Somerville and Winthrop) to chart a Municipal Costs Affordability Index. Below, the chart refers to those communities anonymously, but lists out average property tax and water & sewer bills for the average single-family owner occupied unit in each city in FY'08.
- The data below indicates that municipal charges are less in Chelsea than all other cities.

City	Average Tax Bill	Combined Water & Sewer Bill	Combined Homeowner Costs	% Above Chelsea Cost
A	\$3,571	\$1,307	\$4,878	53.7%
B	\$3,333	\$1,254	\$4,587	44.6%
C	\$3,140	\$1,042	\$4,182	31.8%
D	\$2,980	\$1,194	\$4,174	31.5%
E	\$2,949	\$965	\$3,914	23.4%
F	\$2,961	\$943	\$3,904	23.0%
G	\$2,731	\$674	\$3,405	7.3%
<i>Average</i>	<i>\$3,095</i>	<i>\$1,054</i>	<i>\$4,149</i>	<i>30.8%</i>
Chelsea	\$2,113	\$1,060	\$3,173	

# Conclusion

- The current municipal finance environment, of trouble for the last eight fiscal years and considered by many to be the most severe since the Depression, continues to threaten the viability of municipalities throughout the commonwealth and country.
- Out-year issues continue to be impacted by limited Local Aid growth and growth in non-discretionary spending areas, most notably, Health Insurance and Retirement. The City has played a significant role in raising the statewide debate about these three “Budget Busters.”
- With approximately 59% of the City’s revenue coming from Local Aid, the lagging State budget crisis continues impacting the City’s budget. In FY’09, non-school Local Aid will provide only 96% of that from FY’01. Cumulatively, and not taking into account any loss due to inflation, non-school Local Aid reductions will cost the City \$9.7m from FY’02-’09. Adjusted for inflation, the City is receiving \$2.7m less in Local Aid than would have been anticipated.
- The City saved in “good times” to have Reserves to fund operations in the “bad times.” Those Reserves continue to provide a cushion to allow for a maintenance of service levels while the City’s deficit reduction plans work to eliminate budget deficits in the out-years.
- Central to City’s deficit reduction plans is the development of more than 1,200-units of housing. Absent that, Reserves would be completely exhausted and other deficit reduction plans would be insufficient to bring the FY’11 budget into balance.
- A municipal tax and fee study examining property tax and water & sewer fees for the City and seven neighboring communities finds that the City is the least expensive place to be a single-family owner occupant. With no local Proposition 2 ½ Overrides projected, the City’s relative affordability should remain as such, while the City continues to maintain and expand core municipal services.